

EMPLOYER STATUS DETERMINATION
Decision on Reconsideration
Nexterna, Inc.

This is the decision of the Railroad Retirement Board on reconsideration of Board Coverage Decision 03-44, *Nexterna, Inc.*, which determined Nexterna, Inc. to be an employer under the Railroad Retirement Act (45 U.S.C. § 231 et seq.) and the Railroad Unemployment Insurance Act (45 U.S.C. § 351 et seq.), hereinafter sometimes referred to as “the Acts”. As explained in detail below, a majority of the Board finds on reconsideration that Nexterna was covered under the Acts as a company under common control with a rail carrier employer which provided services in connection with the transportation of property by rail, for the period December 15, 1998 through January 15, 2003, but only with respect to the segregable portion of its workforce engaged in such services.

I. THE DECISION IN B.C.D. 03-44 *Nexterna, Inc.*

The evidence considered in B.C.D. 03-44 was that Nexterna was incorporated in Delaware in December 1986 as Automated Monitoring & Control International, Inc., but changed its name to Nexterna in 2000. It began business in January 1987, and first compensated employees in February 1987. The company was formed by three investor corporations to conduct a wireless information transmission business. These original investors were Alcatel Canada, a subsidiary of the French state telephone company; Tandam Computers, a computer design and manufacturing firm; and the Union Pacific Railroad (UP RR). A fourth company, Motorola, entered in preliminary discussions but never joined the group. The UP RR originally controlled 50 percent of Nexterna, and on December 15, 1998, acquired the remaining 50 percent ownership.

Prior to the time UP RR acquired 100 percent ownership, the corporate by-laws ensured that no single shareholder had control over the “policies and business” of Nexterna through a mechanism involving three classes of common stock, each with different voting rights, and a “Director supermajority vote” rule contained in Article II, Section 3 of the By-Laws. The Nexterna Board of Directors consistently followed the supermajority provision, particularly when dealing with the budget process, spending practices, and other financial issues. Tandem and Alcatel actively participated in all significant policy decisions of Nexterna during the years prior to December 15, 1998.

Nexterna began reducing the number of employees in September 2001 due to declining business, and ended operations in January 2003. However, Nexterna continues as a corporate shell through which the parent company of UP RR, Union Pacific Corporation, controls Nexterna’s subsidiary Nexterna FP. Nexterna FP is based in Canada, and Nexterna states that Nexterna FP “has no customers from the rail industry”.

During its period of active operations, none of the corporate directors were involved in day-to-day management, which was conducted by Nexterna's own executive team. Nexterna had its own sales and marketing operations, its own contracting and procurement practices, and separate legal, accounting, and auditing functions, and its own human resources operation with separate and distinct policies and practices. None of the members of the executive team managing Nexterna had simultaneous positions with Union Pacific.

As noted above, Nexterna's business was wireless two-way communication, data exchange, and related technology. In this business, Nexterna created, or purchased from others for resale, computer programs ("software"); Nexterna designed, purchased for resale, and to a lesser extent contracted for the manufacture of, related electronic data processing products ("hardware") and wireless transmission equipment. Nexterna installed these systems, and offered on-going customer service and maintenance for them. Finally, Nexterna provided expertise and advice to other companies as a consultant in these fields.

Nexterna attempted to market its products and services to the transportation industry and to other industries. Nexterna's transportation-related business generally used the ARC, a computer specially adapted for use on board a locomotive to monitor functioning and to report data; a satellite antenna provided by Wireless Matrix USA, Inc.; and several software products under the collective title OptiSoft. These computer programs sent and received electronic data such as equipment location and fuel consumption, and electronic communications such as work orders and text messages. More specifically, the software program Opti-Track facilitated maintenance by using an on-board computer to monitor oil, motor temperature, fuel usage, etc. A related system, Opti-Track AVL (for Automatic Vehicle Location) used a map to display location, speed, and other information regarding use of vehicles. OptiFuel remotely monitored fuel usage. Another program was OptiWorkOrder, which enabled railroads to report work in the field including current train arrivals and departures, to send new or updated work order information to the field, to receive updates on completed work, and to manage train and track inventory. OptiPath was wireless messaging middleware¹. The OptiTrac program was also offered under license by Wireless Matrix, a satellite data transmission company. To evaluate a company's potential use of the mobile resource management provided by Nexterna's products, the company also developed a computer program entitled Mobile Resource Management.

During 2000 and 2001, Nexterna installed OPTI-Track and related hardware in about one-half of Union Pacific's line haul locomotives, with total installations numbering

¹ Middleware is software that connects two otherwise separate software applications. Common middleware categories include database access programs and message passing. webopedia.com.

2,879. Nexterna submitted bids to Union Pacific to obtain these contracts, and conducted arms-length bargaining with Union Pacific which did not result in better terms for Nexterna than Union Pacific allowed unaffiliated competitors. Nexterna continued to provide limited consulting and servicing of the equipment into 2002. In addition to UP RR, Nexterna provided services to Burlington Northern, Canadian National, Canadian Pacific, CSX, Norfolk Southern, and others.

Nexterna also developed or purchased computer applications for sale to non-rail customers. The company invested \$50 million for products called FreightQuest and FieldPro. The FreightQuest software tracking system allowed customers in the commercial trucking industry to track the status of their shipments. The FieldPro group of computer software applications was sold to a variety of industries, other than railroads, which had significant field services or remote employees. FieldPro provided "an electronic interface for connecting the FieldPro service management system with financial and Enterprise Resource Planning applications." FieldPro Escalations tracked the status of field service calls and automatically notified technicians, dispatchers, managers, or customers of status changes; FieldPro Service Projects provided support for managing projects; Antenna Tools for FieldPro was a web-based application to use FieldPro service management on the internet; FieldPro Remote Tech enabled technicians to download service order dispatches and upload completed work orders and expense reports through a lap-top computer; FieldPro Sales Order Entry supported sales and distribution with packaging, pricing, quotations, orders, shipping, and billing; FieldPro Message Centre was "an integrated communications hub for managing contacts with customers, technicians, vendors and other groups who interact with [the] service team;" the FieldPro Business Intelligence software program helped measure trends, monitor performance indicators, and investigate sources of performance variation. Other related programs were FieldPro Service Inventory and FieldPro IVR Module.

During the years Nexterna was wholly owned by UP RR, the percentage of total sales made to Union Pacific, to the railroad industry, and to other companies is shown below:

<u>Year</u>	<u>% sales to UP RR</u>	<u>% sales to RR industry</u>	<u>% sales to non-RR</u>
1998	28	87	13
1999	58	97	3
2000	80	94	7
2001	80	92	8
2002	43	77	23
1998-2002 average:	58%	89%	11%

Nexterna recruited most of its employees from outside the railroad industry. In 1987, 100 percent of its employees worked in providing services to rail carriers. In 1990, 95 percent provided service to rail carriers; in 1995, 80 percent; and in 2000, 40 percent.

Only 13 of Nexterna's employees had previously worked for a railroad, and no employees transferred from UP RR. However, as of the date of the decision in B.C.D. 03-44, UP RR had hired approximately 40 former Nexterna employees who had been released from Nexterna as the company wound down operations.

The Board evaluated the evidence under section 1(a)(1) of the Railroad Retirement Act (45 U.S.C. § 231(a)(1)), which insofar as relevant here, defines a covered employer as:

(i) any carrier by railroad subject to the jurisdiction of the Surface Transportation Board under Part A of subtitle IV of title 49, United States Code;

(ii) any company which is directly or indirectly owned or controlled by, or under common control with, one or more employers as defined in paragraph (i) of this subdivision, and which operates any equipment or facility or performs any service (except trucking service, casual service, and the casual operation of equipment or facilities) in connection with the transportation of passengers or property by railroad * * *.

Sections 1(a) and 1(b) of the Railroad Unemployment Insurance Act (45 U.S.C. §§ 351(a) and (b)) contain substantially similar definitions, as does section 3231 of the Railroad Retirement Tax Act (26 U.S.C. § 3231).

Section 202.4 of the Board's regulations provides that:

A company or person is controlled by one or more carriers, whenever there exists in one or more such carriers the right or power by any means, method or circumstance, irrespective of stock ownership to direct, either directly or indirectly, the policies and business of such a company or person and in any case in which a carrier is in fact exercising direction of the policies and business of such a company or person. (20 CFR 202.4)

The Board determined that Nexterna was under common control with a carrier by rail effective December 15, 1998, the date UP RR acquired 100 percent ownership.

Section 202.7 of the Board's regulations defines "service in connection with transportation of passengers or property by railroad" as follows:

* * * service rendered or the operation of equipment or facilities * * * is in connection with the transportation of * * * property by railroad, or the receipt, delivery, elevation, transfer in transit, refrigeration or icing, storage, or handling of property transported by railroad, if such service or operation is reasonably directly related, functionally or economically, to the performance of obligations which a company or person or companies or persons have undertaken as a common carrier by railroad, or to the receipt, delivery, elevation, transfer in transit, refrigeration or icing, storage, or handling of property transported by railroad. (20 CFR 202.7).

Because Nexterna designed, sold, and serviced computer software and hardware installations which were reasonably directly related to the performance of obligations undertaken by rail carriers, the Board determined in B.C.D. 03-44 that Nexterna provided a service in connection with rail transportation. Consequently, the Board unanimously found Nexterna to be a covered employer under the Acts effective December 15, 1998, the date it came under common control with the UP RR.

Regulations of the Board provide that coverage of an entity terminates when the company loses any of the characteristics essential to the existence of a covered status. 20 CFR 202.11. The Board unanimously found that Nexterna ceased to be a covered employer January 15, 2003, when it "transferred its rail-related operations" to UP RR.

II. EVIDENCE ON RECONSIDERATION

In support of its request that the Board reconsider B.C.D. 03-44, Nexterna has submitted twelve exhibits. Some of the material consists of copies of documents previously considered by the Board. Reconsideration exhibit 1, June 19, 2002, private placement memorandum for Nexterna series A convertible preferred shares was submitted by Nexterna's letter of August 6, 2002. Nexterna's reconsideration exhibit 2 is the company's letter of September 19, 2000, responding to an inquiry from the Board's Audit and Compliance Section, including "marketing materials" Nexterna attached to describe the above-mentioned computer applications.

The remaining Nexterna reconsideration exhibits present new documents. Exhibits 3 and 4 are patent abstracts. Exhibit 5 is a marketing plan developed prior to the company's name change. Exhibit 6 has three parts: an August 2000 notice terminating the company's "restricted growth plan", a copy of that plan, and a description of the new "year 2000 Nexterna bonus incentive plan". Exhibit 7 is an April 2000 letter from the Colletti Fiss management consulting firm, proposing a new sales incentive compensation plan. Exhibit 8 is an explanation of the plan developed. Exhibit 9 is a chart summarizing the compensation of executives by three business units: field services, rail, and transportation. Exhibit 10 is a group of 20 questionnaires selected by Nexterna from a total of 78 which were completed by Nexterna employees in March

2000 as part of the company's assessment of positions. Exhibit 11 charts the percentage of time which each of the 78 employees returning the survey reported that they spent on the tasks comprising their position. Exhibit 12 lists all employees hired by Nexterna between January 4 and December 27, 2000, including job title and department within the company.

In the statement of facts Nexterna presented in its July 15, 2004 request for reconsideration, Nexterna noted that Nexterna FP is based in Burlington, Ontario, Canada. At a meeting between Nexterna and Board staff at the Board's headquarters building in Chicago on March 14, 2005, Nexterna informed the Board that Nexterna FP has never had employees within the United States. After a search of records following the meeting, Nexterna provided by e-mail dated August 2, 2005, a record showing all Nexterna FP employees for 2000, when Field Pro was acquired, to be residents of the Canadian province of Ontario.

III. ANALYSIS

Nexterna raises three arguments which it contends favor reconsideration and reversal of the Board's initial decision. First, Nexterna states that its primary business was the "manufacture" of computer programs and related hardware, and that manufacture of products is fundamentally different from a "service" performed in connection with transportation by railroad. Reconsideration letter, July 15, 2004, pp. 12-19. Second, Nexterna argues that even if manufacture may generally be considered a service, the manufacture of computer programs and hardware by Nexterna in particular is not a service "in connection with" railroad transportation. Reconsideration letter, pp. 19-22. Finally, Nexterna argues that as most of its staff time was spent in developing and marketing products outside the railroad industry, if Nexterna was a covered employer at all, it was covered only with respect to those employees engaged in railroad-related activities. Reconsideration letter, pp. 22-28. A majority of the Board disagrees with the first and second arguments, but concurs with the third.

A. Manufacturing as a service.

The Board previously addressed Nexterna's first and second arguments in the initial determination of Nexterna's status as an employer. In considering whether manufacturing may be considered a service in connection with rail transportation, we compared the General Counsel's decisions in *Carnegie-Illinois Steel Company*, Legal Opinion L-39-811; *Wheeling Steel Corporation*, L-39-571; *Pullman-Standard Car Manufacturing Company*, L-40-403; and *Ford Motor Company*, L-40-304, with the Eleventh Circuit's decision in Railroad Concrete Crosstie Corporation v. Railroad Retirement Board, 709 F.2d 1404 (11th Cir. 1983). We noted that each of the subject companies in the General Counsel's opinions were found not covered employers because they engaged in the general manufacture of products which were sold in

substantial amounts to “nonaffiliated customers both in and outside the railroad industry.” B.C.D. 03-44 at p. 14. Of particular note among these, Pullman Standard made railroad cars, car parts and accessories, but conducted “most of their business * * * with unaffiliated railroad and non-railroad companies.” See L-40-403. By comparison, Railroad Concrete Crosstie Corporation sold to its rail carrier affiliate 90 percent of the railroad ties it made. 709 F.2d at 1407. In our initial decision regarding Nexterna, we concluded these authorities meant at least that:

* * * where the product manufactured is integral to rail transportation and where the amount of business done with the rail affiliate is not insubstantial, * * * manufacturing may constitute a service in connection with rail transportation. B.C.D. 03-44, at p. 14.

Nexterna responds on reconsideration that in reaching this conclusion, the Board significantly departed from prior agency decisions, citing *Pabtex, Inc.*, B.C.D. 95-112. As recounted in that decision, purchasers of raw coke shipped the material over the affiliated railroad to the Pabtex facility, where Pabtex crushed, graded, blended, and sometimes stored the coke until the purchaser resold it. The owners of the material paid Pabtex directly for these services. In reaching the conclusion that Pabtex was not a covered non-railroad affiliate employer, the decision noted that Pabtex's operations were “analogous to a manufacturing operation and not rail-related services”. In footnote 6, to B. C.D. 03-44 we added that to the extent this language in *Pabtex* suggests manufacturing cannot be a service in connection with rail transportation, we will not follow it. A majority of the Board does not see this statement as the departure from precedent which Nexterna would make of it, for two reasons.

First, the facts in *Pabtex* make it clear that Pabtex served not the railroad, but the purchasers of the coke, with which it contracted, and whose material it refined and stored. These arrangements with non-rail carrier customers, and not the fact that Pabtex was a manufacturer per se, were the basis for the Board decision that Pabtex was not a covered employer. Second, it is the language in *Pabtex*, and not our decision regarding Nexterna, which is contrary to the most venerable pronouncement of the Board on the question of when manufacturing is a service in connection with rail transportation. See: *In the Matter of Lenoir Car Works*, Board Order 39-291, issued May 6, 1939, adopting the report to the Board by the agency's General Counsel acting as Examiner, issued as Legal Opinion L-39-873.

As recounted in the Examiner's findings of fact, Lenoir Car works was a subsidiary of the Southern Railway Company. Though it had earlier repaired Southern Railway locomotives and cars, for several years prior to the decision Lenoir had only manufactured parts for railroad cars and locomotives. Lenoir contended that an affiliated company performed a “service in connection with transportation” by rail only when engaged in actual transportation, or “practically actual transportation” such as the

simple maintenance termed “running repairs” by the rail industry. L-39-873 at 11. In defining the term “service in connection with” the Board first found that “the ordinary usages of language necessarily implies a service that may or may not be itself transportation” and hence reference to legislative history for explanation of the term was unnecessary. *Id.* at 12. Even if reference to legislative history of the 1937 Railroad Retirement Act were justified, the Board found that Congress intended to include “not only activities which are ‘transportation’ as defined in the Interstate Commerce Act, which [definition of] ‘transportation’ [itself] includes more than actual transportation or movement, but also activities which are ‘services in connection with’ ‘transportation * * * as [the term is] defined in the Interstate Commerce Act.’” *Id.* at 21. Finally, the Board reviewed cases under the Interstate Commerce Act which considered the cost of manufacturing of parts in determining the reasonableness of transportation rates, and concluded that “the fabrication and supplying parts necessary in keeping Southern equipment in repair constitute the performance of a service in connection with transportation by railroad.” *Id.* at 22.

The rationale of *Lenoir Car Works* formed the basis for the subsequent June 27, 1939, decision of the Board in *Despatch Shops, Inc.*, Board Order 39-429, ultimately affirmed in the twin Court of Appeals decisions by that name. See: *Despatch Shops, Inc. v. Railroad Retirement Board*, 153 F. 2d 644 (D.C. Cir. 1946)(held an employer under the Railroad Unemployment Insurance Act); and *Despatch Shops, Inc. v. Railroad Retirement Board*, 154 F. 2d 417 (2d Cir., 1946)(held an employer under the Railroad Retirement Act). Forty years later, the Board argued the same reasoning supported a determination that Railroad Concrete Crosstie Corporation performed a service in connection with railroad transportation by manufacturing and selling to its affiliated rail carrier 90 percent of its products. The Eleventh Circuit referred to the *Despatch Shops* cases, noting that manufacture and provision of crossties was as essential to a functioning railroad as repair and construction of rolling stock. *Railroad Concrete Crosstie, supra*, 709 F.2d at 1410. A majority of the Board consequently disapproves the language of the *Pabtex* decision to the extent it may be interpreted as a departure from the agency’s historical position that manufacturing and providing a product to an affiliated rail carrier may constitute a service in connection with transportation of property by rail within the meaning of the Railroad Retirement and Railroad Unemployment Insurance Acts.

B. Nexterna’s service in connection with rail transportation.

Aside from the legal issue of whether manufacturing may be a service under the Act, Nexterna’s second argument is that its own activities were not a service in connection with railroad transportation. Nexterna first compares the use of its products by the purchaser railroad to the product in *Railroad Concrete Crosstie*, and argues that its products were not “integral” to railroad operation in the same sense as cross ties because ties are absolutely essential to moving property by rail, but railroads can and

do operate without Nexterna's products. In a most literal sense this statement would appear to be true. Everyone has seen photos of wreckage resulting from a train leaving the tracks, and a train cannot stay on rails not tied together with cross ties. Concrete or wood, railroads must use some version of cross tie.

A majority of the Board considers Nexterna's limited definition of an essential product too extreme for practical application. Nexterna's logic, reductio ad absurdum, would mean that diesel locomotives are not essential to railroads since railroads once did without diesel power by using steam locomotives and even horses, and telephone and radio communications are not essential since railroads once communicated without them by using the telegraph and semaphore flags. Times and the demands of competition change, and what was once innovation becomes essential. In the majority's view, the best evidence of the essential nature of Nexterna's products and services to operation of the UP RR is the railroad's decision to purchase and install Nexterna's products on 2,879 locomotives.

Nexterna also makes a parallel argument by comparing the nature of the products themselves. Because the cross ties in Railroad Concrete Crosstie were unique to railroads, but satellite communications software and equipment are not, Nexterna reasons that the generic nature of the latter products means a company does not perform service in connection with rail transportation by making and selling them to railroads. A majority of the Board believes that the nature of a product sold to a railroad is only part of the equation. Items ranging from roller bearings to diesel motors are indispensable to modern rail transportation, yet are used by other industries as well. Companies manufacturing these items serve both types of industries. But a company may perform a service in connection with the affiliate's rail transportation business when either furnishing a substantial portion of its products to its affiliated railroad, or when furnishing a substantial portion of the needs of the affiliated railroad for its products. It is the provision of the product, not the process of manufacture, which is the service in connection with railroad transportation.

In favor of reconsideration, Nexterna further argues that it should not be considered to perform a service in connection with rail transportation because the company business plan oriented away from the railroad industry, and in time most of its employees were engaged in developing, servicing and selling products not related to railroads. Case law supports measuring service to an affiliated rail carrier either by staff time or in revenue. Thus, in Interstate Quality Services v. Railroad Retirement Board, 83 F.3d 1463, 1465 (D.C. Cir. 1996), the Court of Appeals for the District of Columbia Circuit affirmed a decision of the Board based on percentage of time the employer's staff spent loading, unloading and storing freight over a four year period (63 to 87 percent for railroads, and 36 to 56 percent for the affiliate). In a case under the analogous provision of the Railroad Retirement Tax Act, the Seventh Circuit found that a company which maintained a building approximately half occupied by the affiliated railroad did not

perform a service, apparently based on factors which included the percentage of janitorial service attributable to space occupied by the railroad. Standard Office Building Corp. v. U.S., 819 F. 2d 1371, 1379 (7th Cir., 1987). On the other hand, Railroad Concrete Crosstie measured the service by percent of sales (90 percent to the affiliated railroad), and the car rebuilding service in Livingston Rebuild Center v. Railroad Retirement Board, 970 F.2d 295 at 296 (7th Cir. 1992), was stated as a percent of Livingston's "business" (95 percent for railroads, including 25 percent for the affiliated railroad).

The evidence in this case is unclear regarding the proportion of employees engaged in non-railroad activity over the 1998 – 2003 period because various measurements seem to conflict. Nexterna's reconsideration letter states (page 11) that in 1999 and early 2000, it had "about 80" employees, and then as part of "a concerted effort to research and develop new wireless technology and market that expertise to new customers and industries, Nexterna increased its workforce to more than 200 employees". Though Nexterna states these new hires did not work in rail related business, there is no evidence bearing directly upon how many of these 80 employees engaged in the rail-related work in 1998 and 1999 prior to the company's new business plan, or whether they continued to work in rail-related work afterward. In 1995, three years prior to the coverage period, Nexterna has stated 80 percent of its employees worked in rail-related activities. Nexterna on reconsideration has charted responses to a "Position Review" questionnaire completed by its employees in March 2000. (Exhibit 11 to July 15, 2004 and July 15 letter at 10). Nexterna argues the chart shows "Only 3 people even mentioned their work with rail as part of their duties." (July 15 letter at 11). On the other hand, Nexterna has also provided a list of 35 individuals hired before 2000 who spent, according to Nexterna, "a considerable amount of time" working with rail industry customers. Acquisition of the above-described FieldPro computer program in June 2000 and the FreightQuest program in May 2001 does support Nexterna's claim that the company went in a new direction after 1999. See: July 15 letter at 7. Yet, as late as December 2000, Nexterna reported that 40 percent of its then-current total of 178 employees (which would be 71 individuals) were "connected with rail." See: attachment to December 7, 2000 letter to the Board's Chief of Audit and Compliance. Finally, when Nexterna ceased non-rail business and folded its rail business into UP RR in January 2003, Nexterna states that UP RR "hired 40 Nexterna employees." (July 15 letter at p.15).

Evidence of staff time ranging back six years ago for a now defunct operation is too uncertain to provide basis for a sound decision. A majority of the Board finds therefore that on the record before us, the percentage of Nexterna's business conducted with the UP RR and other railroads is the clearest and best measure for purposes of determining whether it performed a service in connection with rail transportation. In the majority's view, whether Nexterna actually performed a service in connection with rail transportation must be decided not on hopes of future sales which never materialized,

but on the record of the company's actual performance from the time it came under common control to cessation of operations. As summarized by the table above, the evidence shows for most of the time during which Nexterna was under common control with the UP RR, the majority of its revenue came from provision of products and services to the railroad industry, and further, that most of that revenue came from the UP RR itself.

The Management Member argues that the majority is using the wrong analytical framework in deciding this appeal. He argues that the proper framework is the one set forth in CSX Intermodal, Inc., B.C.D. 96-82. Using this analysis, the Management Member contends that Nexterna should not be considered to be performing a service in connection with rail transportation because the focus of the company was to have significant sales to customers outside the rail industry. CSX Intermodal, Inc. was a second-tier subsidiary of CSX Corporation, Inc. It marketed intermodal services to shippers providing door-to-door shipment under single bill of lading. It would purchase the services of CSX Transportation, an affiliated company, for the rail portion of the movement, if it were advantageous to the shipper.

Although the CSX Intermodal decision is useful in analyzing the status of a carrier's subsidiary, where that subsidiary is engaged in significant non-rail business, the majority believes that it is not useful in Nexterna's case. This is because Nexterna's goal of significant non-rail related sales was never achieved. Its only successful business segment was rail-related sales and service. We need not venture as to whether the result in this case would have been different had Nexterna achieved its goals, since this never happened.

For the foregoing reasons, a majority the Board on reconsideration concludes again that in providing computer programs, satellite communication equipment and computer components Nexterna provided a service in connection with the railroad transportation.

C. Segregation of rail-related service.

A finding that Nexterna did perform services does not necessarily lead to the conclusion that all employees of Nexterna need be reported to the Board as covered employees. As discussed below, a majority of the Board agrees with Nexterna's final argument that on reconsideration, it should be found to be an employer only with respect to the employees engaged in rail-related services.

As Nexterna points out in the reconsideration request, regulations of the Board at 20 CFR 202.9(a) provide that where a company performs a service in connection with railroad transportation but is principally engaged in some other business, the Board will consider whether some identifiable and separable enterprise conducted by the company

may be considered to be the employer covered by the Acts. That regulation states that a determination will be made

* * * in light of considerations such as the following:

- (1) The primary purpose of the company on and since the date it was established;
- (2) The functional dominance or subservience of its business which constitutes a service or operation of equipment or facilities in connection with the transportation of passengers or property by railroad in relation to its other business;
- (3) The amount of its business which constitutes a service or operation of equipment or facilities in connection with the transportation of passengers or property by railroad and the ratio of such business to its entire business;
- (4) Whether such service or operation is a separate and distinct enterprise;
- (5) Whether such service or operation is more than casual, as that term is defined in 202.6.

In considering the evidence regarding Nexterna, a majority of the Board is cognizant of comments by the Seventh Circuit Court of Appeals in Standard Office Building v. United States. In that decision, the Court found that where the railroad used neither a small portion nor almost all of the affiliated company's facilities, under the Railroad Retirement Tax Act "The best approach in the circumstances * * * is one that will minimize corporate reorganizations designed to avoid railroad retirement tax liability and will protect reasonable expectations [of the railroad and the employees]." 819 F. 2d at 1379. Later, in Livingston Rebuild Center, the same Court said that by "presuming that 'railroads' are parts of are distinct entities" when in fact "today, many railroads are part of conglomerates, * * * an attempt to isolate 'the railroad' in the larger enterprise is bound to cover at once too much and too little." 970 F. 2d, at 298. Moreover, it has been held that an individual may jointly be an employee of a covered and non-covered employer. United States v. Pacific Electric Railway Co., 157 F. 2d 902 (9th Cir., 1946)(half of compensation of employees of motor coach service jointly operated by covered rail carrier and non-covered streetcar company was taxable as service to covered employer under the Railroad Retirement Tax Act).

There is no evidence that Nexterna or UP RR in any way sought to avoid coverage under the Acts administered by the Board. In fact, most remaining employees of Nexterna appear to have been transferred to covered positions in the railroad itself at cessation of operations. There is evidence of record showing that at some time the majority of staff time was devoted to non-railroad related work, and that the company devoted considerable resources to the two non-rail related computer systems, FieldPro and Freight Quest. In its submission on reconsideration, Nexterna has identified a

group of employees hired before year 2000 who "spent considerable time working with rail industry customers". (July 15 letter at 25-26.) Moreover, by the end of 2001, Nexterna had reorganized into the Rail Business Unit, the Transportation Business Unit, and the Field Services Business Unit. (Exhibit 1 to July 15 letter, at pp. 5-6). The most recent evidence furnished August 2005 is that since acquisition of the Field Pro program in June 2000, the employees related to the Field Services portion of the business were Canadian residents, working in Canada. The Board has previously determined that service performed by Canadian residents in Canada to a United States employer is not covered service under the Acts. See: Board Order 86-59, *Appeal of Railway Labor Executives' Association Re Canadian Service*, affirmed *Railway Labor Executives' Association v. Railroad Retirement Board*, 842 F. 2d 466, (D.C. Cir. 1988). Service to a Canadian employer, irrespective of the residence of the employee in the United States or Canada, is only covered when performed within the United States. See regulations of the Board at 20 CFR 203.5

This evidence tends to support a conclusion that although Nexterna's revenue demonstrates it served UP RR and the rail industry, company staff primarily engaged in the broader field of computer programs, satellite communications and related hardware. Some of these were Canadian residents performing services in Canada which would not be covered as service in any case. Accordingly, based on the circumstances of this case and in light of the afore-mentioned authorities, a majority the Board is of the opinion that those employees engaged in rail-related activities for the portion of Nexterna which ultimately became the Rail Business Unit constitute an identifiable and separable enterprise conducted by the company.

In conclusion, a majority the Board finds on reconsideration that Nexterna Inc., was a covered employer under the Acts as a company under common control with a rail carrier employer which provided services in connection with the transportation of property by rail, for the period December 15, 1998 through January 15, 2003, only with respect to the employees of the Rail Business Unit and its predecessor employee

groups. The employer is ordered to file appropriate returns of service and compensation for these employees under section 9 of the Railroad Retirement Act and section 6 of the Railroad Unemployment Insurance Act.

Original signed by:

Michael S. Schwartz

V. M. Speakman, Jr.

Jerome F. Kever (Dissenting, separate
Dissenting opinion attached)

**JEROME F. KEVER
MANAGEMENT MEMBER
DISSENT**

NEXTERNA, INC

DECISION ON RECONSIDERATION

I respectfully dissent from my fellow Board Members concerning their determination on reconsideration. I find Nexterna, Inc.'s products and services, which were sold to its affiliated carrier, not to be service in connection with transportation. A review of Nexterna's operations and business plans dictates a different result than the majority's decision.

In a February 23, 2006 submission, Union Pacific Corporation (UP) requested that the Board adopt a modified "paradigm" for analyzing whether Nexterna provided service in connection with transportation as set forth in 45 U.S.C. §231 (a)(1)(ii). This paradigm focuses on factors similar to these set forth in CSX Intermodal, B.C.D. 96-82 citing Lenior Car Works et al, L-38-650. It specifically extends this analysis by reviewing the nature of the service and its relationship to transportation and considers the intended market for the product. The revised analysis is useful when reviewing manufacturing of information technology products and servicing of those products. If this analysis were accepted by the full Board, Nexterna would not be considered a covered employer.

The suggested paradigm, applied on a case-by-case basis, includes review of these factors which I have summarized in terms that I believe the Board should consider: 1) history and origins of the company; 2) company's business objectives; 3) nature of the product and its use in railroading versus non-railroad industry; 4) marketing of products to non-affiliated companies and non-railroad companies; 5) history of whether workers have any previous connection with railroad retirement system or railroad expertise; and 6) physical location of company's office and facilities in relationship to its railroad affiliate.

This expanded approach provides reasonable standards to be considered by companies affiliated with rail carriers who seek to diversify their businesses. Otherwise, a company such as Nexterna, which manufactures and services technology products not integral to railroading, may be subject to reporting requirements and associated contributions should the actual business plan not result in a significant amount of non-affiliated railroad business. Applying the paradigm in this matter would result in Nexterna being found not covered.

History and Origins of the Company

Nexterna was not developed out of the UP Railroad's business. Nexterna was newly formed in 1987 to manufacture and market wireless two-way communication, data exchange and related technology. Additionally, Nexterna provided on-going customer service and maintenance for their systems. Nexterna's incorporators included two non-railroad investors: Alcatel Canada, a subsidiary of the French state telephone company and Tandam Computers, a computer design and manufacturing firm. In December of 1998, the UP acquired one-hundred percent of the outstanding stock of the company.

Company's Business Objectives

As stated earlier, Nexterna was created to manufacture and market wireless two-way communication, data exchange and related technology. The expectations of Nexterna's business plan was to sell to all users of wireless technology including railroads, trucking firms, and companies with significant field services. Nexterna invested close to \$50 million in the non-railroad business. The UP believed that Nexterna could develop in similar fashion to SPRINT, which was formed by Southern Pacific and was eventually spun-off.

While Nexterna's business objectives ultimately were not successful, the nature of the business was comparable to SPRINT. To advance its objectives, Nexterna did considerable research and development and obtained patents, including a patent for collecting and reporting information from mobile assets. Another patent was obtained for a method to route data throughout the country seamlessly without having to sign on each individual wireless network along the way. These are but a few examples of the types of technologies that were being developed by Nexterna. Nexterna was truly a stand alone operation.

The Nature of the Product and its Use in Railroad versus Non-Railroad Industry

The wireless transmission of data is used today by all types of industries. The products sold by Nexterna enhance efficiencies for railroads and all other types of transportation, logistics, or retail businesses. However, the products and services provided by Nexterna were not critical to the railroad's operations; unlike the manufacture of crossties as set forth in Railroad Concrete Crosstie Corp. v Railroad Retirement Board, 709 F. 2d 1404 (11th Cir. 1983). In contrast see, Carnegie Illinois Steel Corporation, L-39-811.

Marketing of Products to Non-Affiliated Companies and Non-Railroad Companies

It was clear that Nexterna did attempt to market to non-affiliated railroads and non-railroad companies. An average of 11 percent of its sales over the period from 1998-2002 were to non-railroad entities. Also, an average of 30 percent of its sales were to non-affiliated carriers.

Based upon the evidence, sales by Nexterna were at arms length to the affiliated carrier giving it no greater bargain than the unaffiliated carriers. This was similar to the facts in CSX Intermodal.

History of Whether Workers Have any Previous Connection with Railroad Retirement System

The vast majority of employees at Nexterna did not have a rail background. Only 13 of a total of 178 employees in the year 2000 had prior railroad service. In fact, many new workers were hired in 2000 as Nexterna began another major push to diversify its business to non-rail users. A significant amount of time was spent by Nexterna's workforce researching and developing these non-rail applications. However, the business plan apparently did not work due to other market forces.

Location of Affiliated Companies Operations

As was the case in CSX Intermodal, Nexterna's operations were separate and apart from the railroads' operations. Nexterna had their own headquarters and associated facilities.

Conclusion

Given the growth and integration of new technology, we can expect that the Board will need to face these issues again in the future. In the instant case, where the entity is no longer in business (Nexterna ceased operations in 2003), this type of approach would be fair since it meets the expectations of the carrier and the employees. Therefore, I would find that the services produced by Nexterna were not integral to railroad operations and would find, based on the totality of facts, that Nexterna was not providing a service in connection with transportation to its affiliated railroad.

Original signed by:

Jerome F. Kever
01/26/07